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SUBJECT: SERBIAN'S ENERGY DEAL WITH RUSSIA POSTPONED

SUMMARY

1. At the April 3rd session, Serbia's caretaker government denied PM Kostunica's proposal to send the draft law on the Serbian-Russian energy agreement to parliament for ratification. Belgrade and Moscow signed the deal on January 25, 2008. The DSS-NS coalition used the failure as a political tool to accuse DS of not working in Serbia's national interest. The deal is now uncertain and may or may not be approved by the new government or ratified by the new Parliament. End Summary.

GAS DEAL ON AGENDA

2. PM Kostunica included the Serbian-Russian energy deal on the April 3rd to be sent to parliament for ratification. In his argument he said that Russia had completed all procedures necessary for the deal to take effect, so Serbia should do the same. Although DSS and NS ministers voted for the energy agreement to be sent for immediate parliamentary ratification, DS ministers abstained, explaining that the caretaker government did not have the authority to approve and propose laws. G17 Plus Minister of Economy and Regional Development Mladjan Dinkic did not attend the session in protest at what he described as Kostunica's attempt to use the deal for election campaigning.

3. At the post-session press conference, DPM Bozidar Djelic from DS and Minister of Trade and Services Predrag Bubalo from DSS debated their interpretations of Serbia's law on the power and authority of a caretaker government to approve draft laws and send them to parliament for ratification. The two, however, did agree that the Russian energy deal was crucial for Serbia, and Djelic said that it would be approved by the new government and ratified by the new parliament. On April 3 Srdjan Mihajlovic, advisor to the NIS General Director, told Econ FSN he expected the energy deal to be one of the main topics of DSS political campaign against DS and that negotiations with Moscow would continue during political campaigning and after elections, especially if democrats win. Mihajlovic believes in order to avoid attacks from DSS Tadic will not block negotiations.

DEAL NOT DEAD

14. Milos Saramandic, the new General Director of NIS from DS confirmed in a conversation with Econ FSN on April 4 that PM Kostunica's DSS party was in a hurry to close the NIS deal. He said General Secretary of the Government Dejan Mihajlov and President of NIS Managing Board Srdjan Bosnjakovic, both from DSS, were Gazprom's main lobbyists and wanted to close the deal before elections, after which a DS victory might lead to DS control of NIS management. Saramandic also said he believed Kostunica included the deal on the agenda knowing it would fail to create an opportunity for DSS to accuse DS and G17 Plus ministers of working against Serbia's national interest.

15. According to Mihajlovic, there is a power struggle over who will control negotiation with the Russians and who will lead key NIS positions. According to Mihajlovic, Gazprom is doing due diligence of NIS thanks to Bosnjakovic's willingness to freely share documents with Gazprom. Bosnjakovic is able to do this while DS members are distracted with an internal battle over who will head key positions within NIS. Reportedly, Saramandic is unsuccessfully trying to channel the flow of documents.

16. Mihajlovic believes DS would try to negotiate with the Russians knowing that it would be hard to change the purchase price of \$570 million, but DS would still fight to increase future investment commitment. DS may also try to reorganize NIS

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and spin-off some of its smaller companies and NIS Naftagas (the domestic production and research division) to sale individually. According to Mihajlovic, DS would offer Gazprom a concession for domestic production and ask for royalty fees. When the concession expires, NIS Naftagas would sell in a tender.

GAZPROM GIVES SERBIA A BLACK EYE

17. During an April 2 lunch at DCM's house to discuss the economic and financial future of Serbia, bankers and academics agreed that the Gazprom deal gave Serbia a black eye in international financial circles. Everyone knew, they said, that NIS was undervalued, that others --including Hungarian and Austrian companies -- had been interested in the tender, and that the sale to Russia was completely political. Privatizations up until the NIS privatization had been done in accordance with modern financial and economic principles, but the Gazprom deal was completely corrupt. They said they thought future investors would be increasingly wary of a level playing field in Serbia, as a result of the Gazprom deal.

COMMENT

18. Although there was much hype surrounding Kostunica's attempt to muscle the Russian energy deal onto the caretaker government's agenda and into parliament, for the most part his short-term goal was seen for what it really was: political

maneuvering and campaigning. The question remains: if the democrats win, will Tadic find the strength to stand up to DSS and negotiate a transparent deal for Serbia's energy resources?

End Comment.

MUNTER